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IN THE

Supreme Court of the United States

(OCTOBER TERM 1949)

CHARLES SIMON and HERMAN T. WARSHOW, as Executors of the Last Will and Testament of EDWARD J. CORNISH, Deceased,

Petitioners,

VS.

JANE M. HOEY, as Executrix of the Last Will and Testament of James J. Hoey, Deceased, formerly Collector of Internal Revenue of the United States of America for the Second District of New York,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

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IN THE

Supreme Court of the United States

(OCTOBER TERM 1949)

CHARLES SIMON and HERMAN T. WARSHOW, as Executors of the Last Will and Testament of EDWARD J. CORNISH, Deceased,
Petitioners,

vs.

JANE M. HOEY, as Executrix of the Last Will and Testament of James J. Hoey, Deceased, formerly Collector of Internal Revenue of the United States of America for the Second District of New York,
Respondent.

No.

TO THE HONORABLE, THE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioners, above named, respectfully pray for a writ of certiorari to the United States Court of Appeals for the Second Circuit to review a judgment of that Court made and entered in the Office of the Clerk thereof on the 30th day of January, 1950, affirming a judgment of the United States District Court for the Southern District of New York made and entered in the Office of the Clerk of that Court on the 10th day of May, 1949, in favor of the respondent and against the petitioners. The District Court judgment, rendered after a trial without a jury, dismissed upon the merits the complaint in an action instituted by the petitioners against the respondent to recover Federal income taxes imposed upon the Estate of Edward J. Cornish, deceased.

The Basis of This Court's Jurisdiction.

The judgment of the Court of Appeals was entered o January 30, 1950. The jurisdiction of this Court is i voked under 28 U. S. C., Section 1254 (1).

The Question Presented, and the Statute Involved.

The question presented by this case and a companio case (*Fred M. Carter and ano. as Executors, etc.* v. *Ja M. Hoey, as Executrix, etc.*) is:

Whether capital gains received by an estate during t period of administration constitute income of the esta within the meaning of Section 162(c) of the Revenue A of 1938; and if so, whether, if such capital gains be proper paid, during the taxable year in which received, to residuary legatee, heir or beneficiary entitled thereto, t amount thereof is to be allowed as a deduction pursua to that Section in computing the net income of the esta for that taxable year.

Section 162(c) of the Revenue Act of 1938 (now Se tion 162(c) of the Internal Revenue Code) reads in fu as follows:

> "Sec. 162. NET INCOME.
>
> "The net income of the estate or trust shall computed in the same manner and on the same bas as in the case of an individual, except that—
>
> • • • • •
>
> "(c) In the case of income received by estat of deceased persons during the period of admini tration or settlement of the estate, and in the ca of income which, in the discretion of the fiduciar may be either distributed to the beneficiary or a cumulated, there shall be allowed as an addition deduction in computing the net income of the esta or trust the amount of the income of the estate trust for its taxable year, which is properly pa or credited during such year to any legatee, hei

or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary."
(52 Stat. 517, 518; 53 Stat. 66, 67)

It has been held below in this and the companion case that since, under New York law, these capital gains are not considered to be income the deduction is not allowable under Section 162(c). This holding is in conflict with principles laid down by this Court in *Lyeth* v. *Hoey*, 305 U. S. 188, as will hereafter appear.

Statement of the Matter Involved.

The related sections of the Revenue Act of 1938 which with Section 162 prescribe the rule or scheme of taxation of income of estates of deceased persons in process of administration are as follows:

Section 161(a)(3) reading as follows:

"Sec. 161. Imposition of Tax.

(a) APPLICATION OF TAX.—The taxes imposed by this title upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

* * * * *

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; * * *"
(52 Stat. 517)

Section 22(b)(3), reading as follows:

"Sec. 22. GROSS INCOME.

* * * * *

"(b) EXCLUSIONS FROM GROSS INCOME. The following items shall not be included in gross income and shall be exempt from taxation under this title:

* * * * *

"(3) GIFTS, BEQUESTS, and DEVISES.—The value of property acquired by gift, bequest, devise, or inheritance (but the income from such property shall be included in gross income);"
(52 Stat. 457, 458)

"Gross income" is defined by subdivision (a) of the same section as including "gains, profits and income derived from * * * sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property * * *."

Section 21 of the same Act defines "net income" as follows:

" 'Net income' means the gross income computed under Section 22, less the deductions allowed by Section 23."

The decisions below have so construed the quoted provisions of Section 162(c) as to make their operation wholly dependent upon State law, contrary to the plain Congressional intent. The Courts below have fallen into this error as the result of confusion in the application of two well settled but distinct and unrelated propositions:

1. That Federal, and not State law, determines for all Federal income tax purposes, the taxable character of payments made by executors of estates to residuary legatees.

2. That, because of the use of the word "properly" in the above statute, State law determines whether or not any such payment has been properly made; i.e.: whether the executor or administrator, who receives his authority under State law, has acted within that law in paying out the money.

The decisions below have unjustifiably expanded the second proposition into one which may be stated as follows:

State law determines whether income has been properly paid, and to determine whether an estate is to be allowed

deduction under Section 162(c) we must look to State law for its view of the character of such a payment; in the case of capital gains, wherever State law would consider them to constitute corpus rather than income under rule of property they cannot be properly paid "as income", and no deduction can be allowed to estates for payments thereof to residuary legatees despite the fact that under State law the payments have been properly made in the due administration of the estate according to State law, and despite the fact that capital gains are income for Federal income tax purposes.

The Courts below failed to perceive that the effect of this distorted expansion of the second proposition is to bring it into sharp conflict with the first, whereas the two are in fact wholly compatible.

The result is a complete misinterpretation of Section 162(c) under which the same word "income" six times used herein without elaboration or qualification, is given varying meanings; this despite the fact that the Federal income tax law has defined what is income for Federal income tax purposes, and has included as part of taxable income gains on the sale of assets (Section 22(a) of the Revenue Act of 1938; 52 Stat. 457). The decisions below assume and in effect hold that the Congress when it used the word "income" in the Section for the fifth time used it in a sense wholly different from that in which it was used elsewhere in the Section—namely that as used for the fifth time, it referred only to income as defined by local or State law, which in the State of New York does not include capital gains.

The reasoning of the District Court, and of the Circuit Court, which affirmed on the opinion of the District Judge, involved a construction of Section 162(c) based in part on the Courts' misconception of the effect of Section 22(b)(3).

Accordingly, the Estate of Edward J. Cornish was held

not to be entitled to a deduction of the amount of income in the form of capital gains properly distributed to the personal representatives of the deceased residuary legatee, and the capital gains were held to be taxable to the Estate. The result of this misconstruction of a plainly worded statute is serious inequity arising from the artificial pyramiding into two taxable entities of capital gains beneficially owned by and actually paid over to some seventeen individuals, as will appear in the petition for a writ of certiorari to be presented herewith in the *Carter* case above mentioned.

The Facts.

The facts in this case are not in dispute and are not complicated. For the purpose of focusing the attention of the Court on the critical events we summarize:

Edward J. Cornish died a resident of Putnam County, New York, on May 3, 1938, leaving a will under which, after providing for certain specific legacies, he gave his entire residuary estate outright to his widow, Selina C. Cornish, who survived him. The will contained no express provision for the disposition of income during the period of administration. The widow died a resident of Putnam County on May 18, 1938, leaving a will and two codicils which were admitted to probate in that County, as was her husband's will. Her interest in the Estate of her deceased husband became payable to her Executors, Fred M. Carter and The Chase National Bank of the City of New York.

The Estate of Edward J. Cornish in its first fiscal year ending on April 30, 1939, realized Federal income tax net short-term gain in excess of $504,378.95 by the sale or other liquidation of capital assets. These capital gains were at all times identified and kept by the Executors separate and apart from all capital assets and from all other income of the Estate, having been kept in a separate

bank account until they were in part distributed to the residuary legatee's personal representatives and in part paid to the petitioners as commissions (R. 29, 30, 57, 58). This segregation was entirely consistent with the manner in which the Estate as a whole was administered, as will appear from an examination of the subsequent account of the petitioners filed by them in the Surrogate's Court, Putnam County (Plaintiffs' Exhibit 2-E, R. 29, 56, a certified copy of which has been lodged with the Clerk of this Court, and the printing of which has been dispensed with for the purposes of this application by stipulation filed with the Clerk of this Court).

On March 29, 1939, more than seven months after the issuance of letters testamentary, the petitioners as Executors of the Edward J. Cornish Estate, as permitted by New York law, properly paid $483,126.51, out of the net capital gains of $504,378.95 referred to above to the Executors of the Estate of Selina C. Cornish, the deceased residuary legatee.

This distribution of net capital gains was accompanied by distribution of other income of $43,728.67 and a partial distribution of cash principal of $125,301.74 (Schedules G and M of Plaintiffs' Exhibit 2-E). The three distributions were made by three checks of the Executors sent to the Selina C. Cornish Executors with a covering letter dated March 29, 1939, describing the distributions accordingly (Plaintiffs' Exhibit 2-F, R. 30, 60, 61).

The three payments made on March 29, 1939 were not part of a final distribution of the residuary estate, but were interim distributions, and the Trial Court so found (R. 112).

The Surrogate's Court of Putnam County approved the payments on settlement of the account of the petitioners on November 4, 1940 (R. 31, 87).

In their Federal income tax return for the tax year involved the Executors, pursuant to a ruling of the Com-

missioner of Internal Revenue, included as taxable income net capital gain of $510,120.01, from which there was a deduction of $5,738.28 for stamp taxes on security sales, leaving a net balance of $504,381.73 (R. 32), and did not deduct from that figure the portions distributed to the Estate of the deceased residuary legatee (R. 32). They paid the tax resulting from the inclusion in taxable income of the capital gain without prejudice and under protest.

Refund was demanded, was not allowed and this action was commenced in due course.

Resumé.

In more succinct fashion, these facts may be summarized as follows:

1. The Estate received income in the form of net capital gains during the period of administration or settlement of the Estate.
2. The capital gains were kept in a separate account on the Executors' books, and in a separate bank account.
3. Within the taxable year in which they were received the capital gains were paid as capital gains to the residuary legatee's executors who were specifically advised of the nature of the distribution.
4. The payment was part of an interim and not a final distribution, and was made within the period of the administration of the Estate of Edward J. Cornish.
5. The payment was made more than seven months after the issuance of letters testamentary to petitioners, and was approved by the Surrogate's Court of Putnam County, New York, upon the settlement of the Executors' account.

The above enumeration includes all of the criteria prerequisite to the allowance of the additional deduction under Section 162(c).

It is the wrongful disallowance by the Commissioner of Internal Revenue, and by the Courts below, of the deduction of the amount of the net gains so paid and distributed to the residuary legatee's personal representatives which constitutes the matter involved on this petition.

Comment.

The property bequeathed (the corpus) is not subject to the income tax either while it is in the possession of the Executor or when it is turned over to the beneficiary. The income from the property is subject to the income tax. (Sec. 22(b)(3), quoted at pages 3 and 4, *supra.*)

This Court, referring to a similar provision of an earlier statute said (*Irwin* v. *Gavit*, 268 U. S. 161 at page 167):

> "But we think that the provision of the act that exempts bequests assumes the gift of a corpus and contrasts it with the income arising from it, * * *"

It is clear that the two sections referred to above provide a plain scheme of taxation of income of estates during the period of administration:

(a) The property bequeathed is not taxable income;

(b) The income during the period of administration is taxable income and must be included in the gross income of the Estate;

(c) If such income be properly paid to the benficiary in the taxable year of its receipt, the Estate gets a deduction from gross income and the beneficiary is taxed on such income;

(d) If such income be not so paid, the Estate is taxable on it.

There can be no doubt that the term "gross income" in Section 22(b)(3) and the term "net income" in Section 162(c) both presuppose the inclusion of capital gains in gross income.

Does or can State law operate to change this scheme of the Federal statutes imposing the income tax? State law does no more than regulate the administration of the Estate and determine the destination of income accruing during administration. It is to be paid out to someone at some time. When and to whom is determined by State law, but the person (beneficiary) to whom it is paid is taxed on it by the Federal Government according to its own scheme of taxation. What the State law calls the money, whether capital or income, has no effect on the operation of the Federal Tax Laws.

Special and Important Reasons for Granting the Writ.

As appears in part from the foregoing, and as will more fully appear in the brief to be submitted herewith, the following reasons should impel this Court to grant the writ:

1. The question of the construction of Section 162(c) of the Revenue Act of 1938 has never been settled or passed upon by this Court in connection with the allowance of a deduction of the amount of capital gains paid to a residuary legatee. Thus this case presents an important question of Federal law which should be settled by this Court both in the public interest and in the interest of the Estate of Edward J. Cornish.

The Private Interest.

Virtually nothing need be said to establish the importance of this question to the estate, for the magnitude

of the sum sought to be recovered speaks for itself. As was previously stated the acompanying petition to be presented in the *Carter* case will show how the seventeen persons interested in this Estate and in the Estate of Selina C. Cornish have been injured by lumping together into the two estates the capital gains realized and paid out during the period of administration.

In passing it should be noted that a judgment for the petitioners would not result in any unjust enrichment of any of the ultimate recipients of the capital gains, for under Section 3801 of the Internal Revenue Code the Commissioner would still be able to assess deficiencies against such of the legatees as did not report the gains as taxable income in their individual income tax returns for the year in which they received them.

The Public Interest.

The public interest lies in having a plainly stated taxing statute construed and applied according to the manifest intention of the Congress. The provisions of the statute involved have existed in substantially similar form since as early as 1918, and their basic general purpose appears always to have been to tax the income of estates to residuary legatees properly receiving and enjoying it.

In view of the continuity of the statutory scheme it would seem important that the doubts cast on its efficacy by the decision below should be resolved by consideration of this case by this Court, so that it can be definitively ascertained whether the statute as now written and as it existed in 1939 is an effective expression of the Congressional intent.

2. The Federal question involved in this case has been decided in the Courts below in a fashion in conflict with applicable decisions of this Court (to wit: *Lyeth* v. *Hoey*,

305 U. S. 188 and *Freuler* v. *Helvering*, 291 U. S. 35) which have laid down the principles determinative of this case, although, as above stated, those principles have never been applied by this Court to a situation involving a payment of capital gains to a residuary legatee.

Those principles have been stated at page 4, *supra*, as has the essence of the manner in which they have been misunderstood and misapplied by the decision below.

In the brief submitted herewith we shall discuss the above mentioned decisions of this Court on which we rely and point to the conflict therewith of the decision below.

3. As will appear from the accompanying brief, the decision of the Court of Appeals below is directly in conflict with a dictum of the Court of Appeals of the Seventh Circuit in *Weigel* v. *Commissioner*, 96 F. (2d) 387. Had this case originated in a district embraced within that Circuit, or been appealed to the Court of Appeals in that Circuit, it appears that the petitioners would have been awarded judgment as prayed for in the complaint. In that case, in which it was held that a deduction was not allowable under Section 162(c) of the Revenue Act of 1928 for a distribution of capital gains by executors of an estate to themselves as testamentary trustees, the Court said at page 389:

> "When no testamentary trust is involved it is consistent with the reality of the situation to hold, for purposes of section 162(c) supra, that residuary legatees who receive payments of funds composed both of original assets of the estate and of estate income, receive that portion represented by estate income as income derived from their own property. This follows from the generally recognized rule that the right of a residuary legatee to his distributive share of the personal property of an estate vests at the death of the decedent."

We appreciate that the foregoing falls somewhat short of a showing of a conflict of *decisions* by Courts of Appeals of different circuits, but the cumulative effect of that difference of opinion of the two circuits when added to the other above stated reasons for review by this Court constitute such a showing of special and important reasons as should impel this Court, in the exercise of sound judicial discretion, to review the judgment of the Court of Appeals.

WHEREFORE your petitioners respectfully pray that a writ of certiorari issue out of this Court to the United States Court of Appeals for the Second Circuit, to review its judgment aforesaid, and that on such review the judgment of said Court of Appeals be reversed and judgment be directed in favor of the petitioners against the respondent for the recovery of so much of their claim for refund as is represented by the tax which was paid on $483,126.51 of capital gains distributed to the personal representatives of Selina C. Cornish, deceased, together with interest and petitioners' costs and disbursements.

Dated, April 14th, 1950.

CHARLES SIMON and HERMAN T. WARSHOW,
as Executors of the Last Will and Testament of Edward J. Cornish, deceased,
Petitioners.

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BRIEF IN SUPPORT OF PETITION

The Opinion Below.

Neither the opinion of the District Judge nor the decision of the Court of Appeals, which affirmed on the opinion of the District Judge, has as yet been officially reported. The opinion of the District Judge appears in the Record at pages 114 to 133 inclusive. The decision of the Court of Appeals appears in the Record at page 140.

The Argument.

As stated in the foregoing petition, although the particular question presented in this case has never been settled or passed upon by this Court, it is the contention of the petitioners that the construction of the statute in question by the Courts below is contrary to the meaning of the statute as expressed therein in plain language, to the Congressional intent underlying the statute, and to fundamental and well settled applicable principles laid down by this Court. We shall first restate those principles and show their applicability to this case, next show how the decision below violates them, and finally review the history of Section 162(c) of the Revenue Act of 1938 in the light of the antecedent discussion of applicable principles.

POINT I.

Statement of two fundamental principles applicable to a construction of Section 162(c).

The First Principle.

The first principle is:

> Federal law determines for all Federal income tax purposes the taxable character of payments made by Executors of estates to residuary legatees.

This principle was laid down by this Court in *Lyeth* v. *Hoey,* 305 U. S. 188, where the question involved was whether property received by an heir under an agreement compromising his objections to the probate of a will was taxable to him as income under the Revenue Act of 1932, the Commissioner having claimed that under the law of the State of Massachusetts the property received by the heir did not come within the definition of the word "inheritance" appearing in Section 22(b)(3) of that Act, and that hence the property was taxable to the heir as income under the Federal Income Tax Law. This Court reversed a decision of the Circuit Court of Appeals for the Second Circuit which had held that what the heir had received was taxable income on the ground that the determination of whether property was received by way of inheritance depended upon the law of the jurisdiction under which the taxpayer received it. This Court in its opinion pointed out that the question had been decided differently in various State courts in connection with the application of State laws of taxation. This Court then said (pp. 193, 194):

> "• • • the question whether what the heir has thus received has been 'acquired by inheritance' within the meaning of the federal statute necessarily is a federal question. It is not determined by local characterization.
>
> "In dealing with the meaning and application of an act of Congress enacted in the exercise of its plenary power under the Constitution to tax income and to grant exemptions from that tax, it is the will of Congress which controls, and the expression of its will, in the absence of language evidencing a different purpose, should be interpreted 'so as to give a uniform application to a nationwide scheme of taxation.' *Burnet* v. *Harmel,* 287 U. S. 103, 110. Congress establishes its own criteria and the state law may control only when the federal taxing act by

express language or necessary implication makes i
operation dependent upon state law. *Burnet*
Harmel, supra. See *Burk-Waggoner Oil Assn.*
Hopkins, 269 U. S. 110, 111, 114; *Weiss* v. *Wien*
279 U. S. 333, 337; *Morrissey* v. *Commissioner,* 2
U. S. 344, 356. Compare *Crooks* v. *Harrelson,* 2
U. S. 55, 59; *Poe* v. *Seaborn,* 282 U. S. 101, 109, 11
Blair v. *Commissioner,* 300 U. S. 5, 9, 10. There
no such expression or necessary implication in this i
stance. Whether what an heir receives from t
estate of his ancestor through the compromise of l
contest of his ancestor's will should be regarded
within the exemption from the federal tax shou
not be decided in one way in the case of an heir
Pennsylvania or Minnesota and in another way
the case of an heir in Massachusetts or New Yo
according to the differing views of the state cour
We think that it was the intention of Congress
establishing this exemption to provide a unifo
rule."

What this Court stated in *Lyeth* v. *Hoey* with referen
to Section 22(b)(3) is equally applicable to Section 162(
of the Revenue Act of 1938, and the word "incom
wherever used therein must refer to income as defined
Federal income tax law, and not as defined by State la
and, as shown in the foregoing petition, that includ
capital gains. In fact the District Judge in this case
held. In his opinion he stated (R. 122):

" 'Income' as used in Sections 21 and 22 includ
any gains from the sale of capital assets. *Bowers*
Kerbaugh-Empire Co., 271 U. S. 170. Income
used in Section 162 must also include such gains a
the money realized as a gain or profit by the exe
tors of Edward J. Cornish on the sale of assets
the estate was necessarily income of the Estate
Edward J. Cornish within the definition of
federal statute."

The Second Principle.

The second principle is:

> Because of the use of the word "properly" in Section 162(c) State law determines whether or not any payment of income by an Executor to a residuary legatee has been properly made, i.e. State law determines whether an executor has acted within that law in paying out the money.

The Federal income tax laws do not purport to regulate the administration of estates. This was recognized by this Court in *Lyeth* v. *Hoey* (*supra*), where this Court stated (p. 193):

> "Undoubtedly the state law determines what persons are qualified to inherit property within the jurisdiction. *Mager* v. *Grima,* 8 How. 490, 493; *Maxwell* v. *Bugbee,* 250 U. S. 525, 536, 537. The local law determines the right to make a testamentary disposition of such property and the conditions essential to the validity of wills, and the state courts settle their construction. *Uterhart* v. *United States,* 240 U. S. 598, 603. The State establishes the procedure governing the probate of wills and the processes of administration. Petitioner's status as heir was thus determined by the law of Massachusetts. That law also regulated the procedure by which his rights as an heir could be vindicated. The state law authorized its courts to supervise the making of agreements compromising contests by heirs of the validity of an alleged will of their ancestor, in order that such compromises shall be just and reasonable with respect to all persons in interest."

More specifically the proposition above stated is to be found embodied in the decision of this Court in *Freuler* v. *Helvering,* 291 U. S. 35. That case involved an attempt

by the Commissioner to impose an income tax upon the estate of a deceased income beneficiary of a trust under a will. The Commissioner sought to levy the tax upon the actual amount distributed and paid to the deceased beneficiary, although that amount was in excess of that which was subsequently determined by a State Court decree to have been properly paid to the income beneficiary. This Court held that the State Court decree determined the amount properly paid to the beneficiary, and that that was the only amount of income for which the beneficiary could be taxed. What this Court said in that case with reference to Section 219 of the Act of 1921 is equally applicable to Section 162(c) of the Revenue Act of 1938, and there can be no doubt but that the word "properly" in Section 162(c) relegates us to State law to determine the propriety of any payments by executors to legatees.

The District Judge in the instant case so held, stating (R. 122):

> "The state courts supervise and control the estates of decedents and the conduct of the executors and administrators of the estates. The state courts determine the rights of creditors, legatees and distributees and also the manner and method of payments of the estate to legatees and beneficiaries. Whether an executor may 'properly' pay a sum out of an estate, is a matter to be determined by local law, since its concerns problems over which the state courts exercise jurisdiction in the administration of estates."

The District Judge also quoted with approval (R. 123) a statement in *Proctor* v. *White,* 28 F. Supp. 161 (D. C., Mass. 1929), wherein that Court said with reference to Section 162(c) of the Revenue Act of 1928, at page 165:

> "The words 'properly paid' in the Revenue Acts cited naturally mean rightly paid, with legal justification."

In the instant case the payment of the capital gains was subsequently approved by the Surrogate's Court of Putnam County by its decree settling the petitioners' account (R. 31, Plaintiffs' Exhibit 2-E, Schedule G, 87-92).

POINT II.

Analysis of the error in the decision below.

At the above point in the opinion of the District Judge it would appear that the petitioners were to be awarded judgment. However the decision in this case then turned upon an error having its inception in a misunderstanding of what was decided by this Court in *Burnet* v. *Whitehouse*, 283 U. S. 148. In that case the Commissioner of Internal Revenue sought to include in a taxpayer's taxable income the amount of an annuity received during the taxable year from a decedent's estate on the theory that income of the estate had been used to pay the annuity. The annuitant claimed that the payment received by her was exempt from income tax under the provisions of paragraph (b) item (3) Section 213, of the Revenue Act of 1921, which provided that the term "'gross income' * * * (b) Does not include * * * (3) the value of property acquired by gift, devise, or descent (but the income from such property shall be included in gross income); * * *." It will be noted that this Section is virtually identical with Section 22(b)(3) of the Revenue Act of 1938.

This Court observed that the bequest to the annuitant was not one to be paid from income but of a sum certain, payable at all events in each year of her life, for the will had directed payment without reference to the existence or absence of income, and then stated that the gift did not depend upon income but was a charge upon the whole estate during the life of the legatee to be satisfied *like any ordinary bequest.* This Court stated (p. 151):

> "It would be an anomaly to tax the receipts for one year and exempt them for another simply because executors paid the first from income received and the second out of the corpus. The will directed payment without reference to the existence or absence of income."

The Court rejected the Commissioner's argument that the income actually used to make the payment was taxable to the annuitant under the provisions of Section 219(d) of the 1921 Act, which had provided that in the case of estates or trusts where income was to be distributed to beneficiaries periodically, the income tax should not be paid by the fiduciary, but that there should be included in computing the net income of the beneficiary that part of the estate income distributable to him. In rejecting this argument this Court said of said Section 219 (p. 151):

> "• • • But clearly enough, we think, this section applies only to income paid as such to a beneficiary. And as above shown, the sums received by Mrs. Whitehouse were not gifts to be derived from and paid out of income, nor were they received as such by her.
>
> "The exemption in § 213 is plain and should not be destroyed by any strained construction of general language found in § 219."

In *Helvering* v. *Pardee*, 290 U. S. 365, this Court in another decision involving annuities denied a deduction under Section 219 of the Revenue Act of 1924 to a Trustee for payments of trust estate income to an annuitant, stating briefly (pp. 370, 371):

> "The annuity provided by the will for Mrs. Pardee was payable at all events. It did not depend upon income from the trust estate. She elected to accept this in lieu of her statutory rights. *She chose to assume the position of an ordinary legatee.* Section 213 (b)(3), Revenue Act of 1924, c. 234, 43

> Stat. 253, 267, 268, exempts bequests from the income tax there laid. Payments to Mrs. Pardee by the fiduciary were not necessarily made from income. The charge was upon the estate as a whole; her claim was payable without regard to income received by the fiduciary. Payments to her were not distribution of income; but in discharge of a gift or legacy. The principle applied in *Burnet* v. *Whitehouse,* 283 U. S. 148 is applicable." (Italics ours.)

Without regard to the fact that these two cases involved a particular class of legatee, namely annuitants, whose legacies are charges upon estates as a whole, and who were likened by this Court to "ordinary" legatees (meaning pecuniary legatees) lower courts have assumed that the cases laid down general rules for determining the taxability for Federal income tax purposes of receipts by all kinds of legatees, including residuary legatees, and the deductibility of payments under Section 162(c). They have assumed further that the test is that of whether the payments have been of income "as such" or in other words, of income "as income". The District Judge in this case made the same assumption, saying (R. 122):

> "In calculating the income tax of an estate the Federal statute [§ 162(c)] allows a deduction or exemption to the estate of income, paid as such to legatees or beneficiaries, [Sandborn v. Commissioner of Internal Revenue, 88 F. (2d) 134 (C. C. A. 8th 1937); *Weigel* v. *Commissioner of Internal Revenue,* 96 F. (2d) 387 (C. C. A. 7th 1938)], only if it was 'properly paid or credited' to the legatee or beneficiary."

If it be assumed that this Court has laid down such a test, we submit that in the case at bar that requirement was met. Here the proof shows that the capital gains were paid to the residuary legatee's personal representatives "as capital gains" as part of a proper interim dis-

tribution of the estate, and that the legatee's personal representatives were advised of the nature of the distribution; since capital gains constitute income for Federal income tax purposes and income within the meaning of Section 162(c), they were paid "as income" or "as such", and the petitioners were entitled to a deduction to the extent of their amount.

This also follows from the generally recognized rule that the rights of a residuary legatee relate back to the date of death of the testator, so that the increment arising on the property of which the decedent died the owner is equitably the income on the residuary legatee's own property. As was said by this Court in *Brewster* v. *Gage*, 280 U. S. 327, at page 334, relative to the rights of a residuary legatee:

> "Upon acceptance of the trust there vests in the administrators or executors, as of the date of the death, title to all personal properly belonging to the estate; it is taken, not for themselves, but in the right of others for the proper administration of the estate and for distribution of the residue. The decree of distribution confers no new right; it merely identifies the property remaining, evidences right of possession in the heirs or legatees and requires the administrators or executors to deliver it to them. The legal title so given relates back to the date of the death. *Foster* v. *Fifield*, 20 Pick. 67, 70. *Wager* v. *Wager*, 89 N. Y. 161, 166. *Thompson* v. *Thomas*, 30 Misc. 152, 158."

More specifically, in connection with Section 162(c) the Court of Appeals of the Seventh Circuit stated in a case involving payments of capital gains by executors to testamentary trustees, in *Weigel* v. *Commissioner*, 96 F. (2) 387, at page 389:

> "When no testamentary trust is involved it is consistent with the reality of the situation to hold, for purposes of section 162(c) *supra*, that residuary

> legatees who receive payments of funds composed both of original assets of the estate and of estate income, receive that portion represented by estate income as income derived from their own property. This follows from the generally recognized rule that the right of a residuary legatee to his distributive share of the personal property of an estate vests at the death of the decedent."

However the Courts below, and other lower Courts on whose decisions the District Judge relied, have added to the proposition that to be deductible under Section 162(c) the payment must be out of income in the hands of the fiduciary the further requirement that it must also be income under State law in the hands of the beneficiary. Under that erroneous test, wherever State law would consider capital gains to constitute corpus rather than income under a rule of property they cannot be properly paid "as income" and the deduction cannot be allowed despite the fact that under State law the payment was properly made in the due administration of the estate, and despite the further fact that capital gains are income for Federal income tax purposes. This, as we have pointed out, is in direct conflict with this Court's determination in the *Lyeth* case (305 U. S. 188).

The erroneous proposition, which we have also attempted to phrase at pages 4-5, *supra,* is not to be found in so many words in the opinion below but is to be gleaned from the following statements in the opinion:

> "The weight of authority is to the effect that a capital gain realized by an estate in the course of its administration, may, in the absence of any specific provision in the will and in the absence of any prohibition in the law of the state in which the estate is being administered, be properly paid as income to residuary legatees of the estate and deducted from the income of the estate under Section 162(c)." (R. 126.)

* * * * *

> "But, *Bank of Richmondville* v. *Graves, supra,* represents the law of the State of New York. It declared unequivocably that capital gain received by an estate becomes a payment of corpus, rather than of income, when distributed to a residuary legatee, and that it is not currently distributable as income. Mindful of the direction of the *Ardenghi* case (*supra*) to resort to local law for a determination of whether the income is 'properly paid' I have concluded that while the capital gains could be properly paid to the residuary legatee as principal, and the Surrogate's decree on the settlement of the executors' accounts approved their payment as a payment of principal, the capital gains could not, under the *Richmondville Bank* case, be 'properly paid' to the residuary legatee as income. For the foregoing reasons I have also concluded that Section 162(c) of the Revenue Act of 1938 providing for a deduction of income, 'properly paid', does not authorize a deduction from the taxable income of the Edward J. Cornish Estate of the capital gains paid by the executors of that estate to the residuary legatee, the estate of Selina C. Cornish, because under the New York law the capital gains could not be 'properly paid' to the residuary legatee as income." (R. 132.)

And in his opinion in the *Carter* case, the District Judge said (*Carter* R. 188, 189):

> "Under the law of New York the estate of Selina C. Cornish received that distribution as a legacy under her husband's will. It was part of the corpus of his estate when paid out to her estate, and as to her estate was exempt from any income tax thereon pursuant to Section 22(b)(3) of the Revenue Act of 1938."

The erroneous proposition may also be found in other cases disallowing a deduction for payments of capital gains by executors *to testamentary trustees,* e.g.:

Weigel v. *Commissioner*, 96 Fed. (2) 387, wherein the Court said at page 391:

> "The act does not define 'properly paid or credited' and 'properly paid or credited' must be taken to mean properly paid or credited as income. For if it is properly paid or credited as a legacy or inheritance under a will it is exempt from income tax as against the legatee or heir under section 22(b)(3) and cannot be included in the computation of the net income of the legatee or heir under section 162(c); and the result would be to transform the deduction authorized by section 162(c) into an exemption. This would defeat the obvious purpose of section 162(c), which is merely to permit the shifting of the liability to account for estate income from executors or administrators to legatees or heirs to whom it has been properly paid or credited."

Burchenal v. *Commissioner*, 150 Fed. (2) 483, wherein the Court said at page 485:

> "But these are not the only prerequisites which must be complied with in order to show that the estate may be entitled to the deduction. It is also necessary to show that the amounts were income, and were 'properly paid or credited as income.'
>
> "(4-6) Clearly the amounts received from an increase in the value of stock, $26,509.94 in 1939, and $11,839.06 in 1940, are capital gains. The Tax Court correctly held that the mere fact that under the revenue laws capital net gain is taxable income does not prevent this gain from becoming part of the corpus of the estate immediately upon its realization. Helvering v. Butterworth, 290 U. S. 365, 370, 54 S. Ct. 221, 78 L. Ed. 365; Burnet v. Whitehouse, 283 U. S. 148, 51 S. Ct. 374, 75 L. Ed. 916, 73 A. L. R. 1534. Such gain is actually part of the corpus of the trust, and it cannot be properly credited as income."

and *In Re Rogers' Estate,* 143 F. (2) 695, wherein the Court said at page 696:

> "2. We also agree with the Tax Court that the capital gain resulting from the sale of decedent's property by the executors was not income of the estate 'paid or credited' to beneficiaries within the meaning of § 162(c), 26 U. S. C. A. Int. Rev. Code, § 162(c). Decedent's will expressly forbade such a result since it provided that 'all realized appreciation in the value of stock * * *, resulting from the sale * * * thereof, shall be considered principal and not income * * *.' Likewise, under the New York decisions, such a gain is regarded as an addition to the corpus of the estate; Bank of Richmondville v. Graves, 259 App. Div. 4, 18 N. Y. S. 2d 133, affirmed 284 N. Y. 671, 30 N. E. 2d 720. In the accounts filed by the executors with the Surrogates they showed these gains as part of the 'principal'."

The foregoing erroneous proposition as applied to this case ignores:

1. The fact that this Court has decided that Federal law determines the taxable character of the payment;

2. The fact that under Federal income tax law the capital gains are income, and hence can be paid "as income", if that be regarded as of any importance;

3. The fact that under Federal tax law the gains are not exempt from income tax in the hands of the residuary legatee because under that law they are not part of the property of which the testator died the owner, i.e. "the corpus", and hence not the property passing by inheritance, but rather are "the income arising therefrom";

4. The fact that the capital gains were determined to have been properly paid by the decree on accounting in the proceeding to settle the executors' accounts;

5. The difference between the nature of the rights of an annuitant or an ordinary legatee on the one hand, and those of a residuary legatee on the other.

POINT III.

The decision below defeats the purpose underlying the enactment of Section 162(c).

As far back as 1918 the Revenue Act contained provisions whereby estates were given a deduction for the amount of the income of the estate properly paid or credited to any legatee, heir, or beneficiary during the period of administration or settlement. Section 219 of the Revenue Act of 1918 reads, so far as pertinent, as follows:

> "(a) That the tax imposed by sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including—
>
> (1) Income received by estates of deceased persons during the period of administration or settlement of the estate;
>
> * * * * *
>
> (c) In cases under paragraph (1), (2), or (3) of subdivision (a) the tax shall be imposed upon the net income of the estate or trust and shall be paid by the fiduciary, except that in determining the net income of the estate of any deceased person during the period of administration or settlement there may be deducted the amount of any income properly paid or credited to any legatee, heir or other beneficiary. In such cases the estate or trust shall, for the purpose of the normal tax, be allowed the same credits as are allowed to single persons under section 216.
>
> (d) * * * in the case of any income of an estate during the period of administration or settlement permitted by subdivision (c) to be

> deducted from the net income upon which tax is to be paid by the fiduciary, the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary his distributive share, whether distributed or not, of the net income of the estate or trust for the taxable year, * * *"
>
> (Vol. 40, Part I, Stat. 1071.)

This is the direct statutory ancestor of Section 162(c) of the Revenue Act of 1938; it appears again with unimportant variations of expression in Sections 219 of the Acts of 1921, 1924 and 1926, and in Sections 161(a) and 162(c) of the Acts of 1928, 1932, 1934 and 1936.

Section 162(c) appears in the Internal Revenue Code today in language identical with that of the Revenue Act of 1938, although by Section 111 of the Revenue Act of 1942 certain rules for its implementation were added and appear in Section 162(d) of the Code. They are of no importance to this case.

After even a casual reading of these statutes, can it be doubted that in the case of residuary legatees, as distinguished from annuitants or pecuniary legatees, the dominant purpose expressed in each of these Acts was to tax the income of an estate to a residuary legatee receiving and enjoying it?

When it appeared to the Congress from a series of lower Court decisions of cases involving distributions of "ordinary" estate income,—i.e. interest, dividends, and the like—on *final* settlement of estates (as distinguished from interim distributions) that estates were not being allowed deductions under Section 162(c) for reasons akin to those stated as the basis of the decision in this case, the Congress took prompt steps to insure that its will should be carried out, and by Section 111 of the Revenue Act of 1942 amended Section 162(b) to overcome those decisions, although it could just as well have done so by amending

162(c). On the basis of the language theretofore used neither section, in our opinion, required amendment for the deduction to have been allowable in cases involving final distribution.

Be that as it may, until the decision in this case no case had ever denied an estate a deduction under Section 162(c) in connection with proven proper interim distributions of either ordinary income or capital gains, except the annuity cases and the cases involving distributions of capital gains by executors to trustees. Denial of the deduction in that latter class of case, however unjustified in strict theory, involves no defeat of the basic Congressional intent, inasmuch as in the normal course capital gains received by a trustee are added to trust corpus, and until the trust terminates are not directly enjoyed by anyone. The very Court whose decision is now sought to be reviewed, and which decided one of those trust cases, to wit, *In Re Rogers Estate, supra,* had itself, in *Weber* v. *Commissioner,* 111 Fed. (2) 766, allowed the deduction in the case of a distribution of capital gains to residuary legatees. True, that same Court in the *Rogers* case said that certain of its expressions in the *Weber* case were dictum. Nevertheless, we quote that dictum, if such it were, because of its inherent logic (p. 768):

> "The gain realized in 1933 was paid over in the same year by the executors to the children. Beyond doubt the payment was 'properly' made, for the children, whether or not they had title to the proceeds, had the right to an immediate distribution. We cannot grasp the Commissioner's argument that the profit on the sale 'was never payable to them as such but was paid to them in discharge of their legacies'. The profit was payable to them as profit, because it was part of the proceeds of sale of the farm. See *Commissioner* v. *Stearns,* 2 Cir., 65 F. 2d 371. On the assumption that it was the estate which realized the profit, the case is squarely within section 162(c)."

In connection with the 1942 amendments above mentioned, the following statement appears in the report of the Committee on Finance of the United States Senate:

> "The question of whether the income of an estate or trust for the taxable year in which it becomes payable as part of an accumulation is taxable on the one hand to the estate or trust or on the other hand to the legatee or beneficiary has been a source of litigation in certain cases under existing law. This amendment is designed to *clarify* the law." (Italics ours.)
>
> (S. R. No. 1631—77th Congress, 2nd Session, Pages 71, 72.)

If we have correctly stated the intent of Congress to be that of taxing the income of an estate to a residuary legatee who receives and enjoys it, what conceivable reason can there be for assuming that Congress intended capital gains to receive any different treatment from other forms of estate income which have in fact been distributed, and what conceivable imperfection of expression is to be found in the statute under consideration to justify a holding such as that of the Court below in this case?

Conclusion.

We respectfully submit that the foregoing demonstrates:

1. That this case presents a Federal question not heretofore settled or passed upon by this Court, and that it is in the public interest that this case be reviewed by this Court so that a plainly stated taxing statute, to wit: Section 162(c) of the Revenue Act of 1938, now Section 162(c) of the Internal Revenue Code, may be construed and applied according to the manifest intent of the Congress.

2. That the Federal questions involved in this case have been decided in the Courts below in a fashion in conflict with applicable decisions of this Court which have laid down the principles determinative of this case.

3. That the decision of the Court of Appeals below is in direct conflict with a dictum of the Court of Appeals of the Seventh Circuit in *Weigel* v. *Commissioner*, 96 F. (2d) 387, in which dictum there appears a correct expression of the law applicable to this case, and that it appears that that Court by the application of the principle stated in the dictum would have awarded the petitioners judgment as prayed for in the complaint.

4. That this Court, in the exercise of sound judicial discretion, should allow the writ.

Respectfully submitted,

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Dated, April 14th, 1950.

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In the Supreme Court of the United States

OCTOBER TERM, 1949

No. 757

CHARLES SIMON AND HERMAN T. WARSHOW, AS EXECUTORS OF THE LAST WILL AND TESTAMENT OF EDWARD J. CORNISH, DECEASED, PETITIONERS

v.

JANE M. HOEY, AS EXECUTRIX OF THE LAST WILL AND TESTAMENT OF JAMES J. HOEY, DECEASED, FORMERLY COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES OF AMERICA FOR THE SECOND DISTRICT OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 114-133) is reported at 88 F. Supp. 754. The *per curiam*

opinion of the Court of Appeals (R. 140) is reported at 180 F. 2d 354.

JURISDICTION

The judgment of the Court of Appeals was entered January 30, 1950. (R. 141.) The petition for a writ of certiorari was filed April 17, 1950. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTION PRESENTED

Whether capital gain realized by an estate in the course of its administration, and distributed to the residuary legatee as part of the corpus of the legacy, is taxable to the estate or to the legatee under Section 162(c) of the Revenue Act of 1938.

STATUTE INVOLVED

Revenue Act of 1938, c. 289, 52 Stat. 447:

SUPPLEMENT E—ESTATES AND TRUSTS

SEC. 161. IMPOSITION OF TAX.

(a) *Application of Tax.*—The taxes imposed by this title upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

* * * * *

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; * * *

* * * * *

(b) *Computation and Payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary * * *.

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * *

(c) In the case of income received by estates of deceased persons during the period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year, which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary.

STATEMENT

The facts as stipulated (R. 27-34) and found by the District Court (R. 114-118) may be summarized as follows:

The decedent, Edward J. Cornish, died a resident of the State of New York on May 3, 1938. By his will he bequeathed his entire residuary estate to

his widow, who survived him by about two weeks. The will was silent as to the disposition of any income earned or realized by the estate during the period of administration. (R. 114.)

During the first fiscal year of the estate, ending April 30, 1939, the executors sold certain assets of the estate, as a result of which the estate realized net capital gains of $504,378.95. These gains were deposited by the executors in a separate bank account. On March 29, 1939, the executors distributed to the widow's estate, as residuary legatee, $483,126.51 of the capital gains. (R. 115-116.)

In October of 1940, the executors filed in the Surrogate's Court of New York an account of their proceedings. In that accounting the capital gain of $504,378.95 realized by the estate was charged to "Principal", and the $483,126.51 distributed therefrom to the residuary legatee was credited to "Principal". The account filed by the executors contained separate schedules relating to "Income", and the capital gain distributed was not included in any of those schedules. The account was judicially settled and allowed as filed. (R. 116-117.)

Prior to filing an income tax return for the estate, the executors requested from the Commissioner of Internal Revenue a ruling as to whether the capital gain distributed to the residuary legatee was taxable to the estate or to the legatee, and the Commissioner ruled that it was taxable to the estate. (R. 93-99, 117.) Thereafter the executors filed a return on behalf of the estate in which the

capital gain was included as income, without deduction for the portion paid to the residuary legatee. A claim for refund was duly filed and, upon its rejection, this suit for refund was instituted. (R. 117-118.)

The executors contended that the amount of capital gain distributed to the residuary legatee was deductible from the estate's income and taxable to the residuary legatee under Section 162(c) of the Revenue Act of 1938, *supra,* p. 3. The District Court held that the amount had been distributed to the residuary legatee as corpus, not as income, and that therefore the estate rather than the legatee was taxable on the amount under Section 162(c). (R. 118-133.) The Court of Appeals affirmed *per curiam.* (R. 140.)

ARGUMENT

1. By Sections 161 and 162 of the Revenue Act of 1938, *supra,* pp. 2-3, a decedent's estate is treated for income tax purposes substantially the same as an individual with respect to income realized during the period of administration. However, Section 162(c), *supra,* provides that in computing the net income of the estate there shall be allowed as an additional deduction "the amount of the income of the estate * * * which is properly paid or credited * * * to any legatee * * * but the amount so allowed as a deduction shall be included in computing the net income of the legatee * * *."

The plain purpose of Section 162(c) is to tax income realized by an estate during the period of administration either to the estate or to the legatees. If the income is "properly paid or credited" to a legatee as "income", it is deductible by the estate and includible in the gross income of the legatee. On the other hand, if it is distributed to the legatee as part of the principal or corpus of the legacy, it is taxable to the estate rather than to the legatee. As several circuits have already held, the issue of whether estate income is distributed to the legatee as income, or as corpus, depends on the terms of the will and the law of the state where the estate is being administered. *In re Rogers' Estate,* 143 F. 2d 695, 696 (C. A. 2), certiorari denied, 323 U. S. 780; *Anderson's Estate* v. *Commissioner,* 126 F. 2d 46, 47-8 (C. A. 9), certiorari denied, 317 U. S. 653; *Burchenal* v. *Commissioner,* 150 F. 2d 482, 485 (C. A. 6); *Dunlop* v. *Commissioner,* 165 F. 2d 284, 287 (C. A. 8); cf. *Burnet* v. *Whitehouse,* 283 U. S. 148; *Helvering* v. *Pardee,* 290 U. S. 365; *Ardenghi* v. *Helvering,* 100 F. 2d 406 (C. A. 2), certiorari denied, 307 U. S. 622.

The estate income here in question consists of capital gains distributed to a residuary legatee. The will is silent as to the disposition of income realized by the estate during administration, and under the law of New York, where the estate is being administered, a distribution of capital gain by an estate to a residuary legatee constitutes a

distribution of corpus, not of income. *Bank of Richmondville* v. *Graves,* 259 App. Div. 4, affirmed, 284 N. Y. 671; *In re Rogers' Estate,* 143 F. 2d 695, 696 (C. A. 2), *supra.* Moreover, the executors accounted for the distribution as a payment of principal, and the distribution was judicially approved by the Surrogate's Court as such. (R. 114-117.) Applying the provisions of Section 162 (c) and these established principles, the courts below correctly held that the capital gain was taxable to the estate rather than to the residuary legatee, since it was paid to the legatee as principal and not as income.

The contentions made by the estate in its petition for certiorari are essentially the same as those advanced in the petitions for certiorari in the *Rogers' Estate* and *Anderson's Estate* cases, *supra.* Nothing has occurred since the denial of certiorari in those cases which calls for further review of this case.

2. Taxpayer's assertion of conflict (Pet. 11-12, Br. 15-16) with *Lyeth* v. *Hoey,* 305 U. S. 188, is without substance. This Court there held that "property" received by an heir from an estate, in compromise of a will contest, was acquired by "inheritance" within the meaning of Section 22(b)(3) of the Revenue Act of 1932, c. 209, 47 Stat. 169, which excluded from the definition of gross income (as contained in Section 22(a)) "The value of property acquired by gift, bequest, devise, or in-

heritance". Accordingly, it was held that the property was not includible in the gross income of the heir. Far from being in conflict with the *Lyeth* case, the decision below is in harmony with it. Since the amount here in question was distributed to the residuary legatee as corpus ("property"), the courts below properly held that it was not taxable to the legatee, but to the estate. See *Anderson's Estate* v. *Commissioner,* 126 F. 2d 46 (C. A. 9), certiorari denied, 317 U. S. 653, and the other cases cited *supra,* p. 6.

True, as taxpayer emphasizes, this Court in the *Lyeth* case held that what is includible or excludible as taxable income is governed by the federal taxing statute, not by local law. But we are not here concerned with the question of *whether* the income is subject to tax; admittedly the capital gain in question constitutes taxable income either to the estate or to the legatee. Rather, we are here concerned with *who,* as between the estate and the legatee, is taxable on that income. Under Section 162(c) of the federal taxing statute, the answer depends upon whether the income was "properly paid" to the legatee as "income", or as corpus. Here, as in other instances, the controlling federal statutory provision by "necessary implication" makes the tax incidence turn on the terms of the will or trust as interpreted by the applicable state law. *Helvering* v. *Stuart,* 317 U. S. 154, 161-163; *Freuler* v. *Helvering,* 291 U. S. 35; *Burnet* v. *Whitehouse,*

283 U. S. 148; *Blair* v. *Commissioner,* 300 U. S. 5. Thus, in *Burnet* v. *Whitehouse, supra,* this Court held that even though an amount distributed by a testamentary trust represented trust income, it was not taxable to the beneficiary because under the terms of the will it was a charge upon the whole estate and thus was paid as corpus. In the instant case the capital gain which the executors distributed to the residuary legatee likewise was paid as corpus.[1]

3. Nor is the decision below in conflict with *Freuler* v. *Helvering,* 291 U. S. 35, as taxpayer asserts. (Pet. 11-12, Br. 17-18.) On the contrary, this Court there held (pp. 43-45) that local law was determinative of whether trust income was "distributable" to a beneficiary within the meaning of Section 219 of the Revenue Act of 1921, c. 136, 42 Stat. 227, the predecessor of Section 162 of the Revenue Act of 1938 here involved. As for *Weigel* v. *Commissioner,* 96 F. 2d 387 (C. A. 7), upon which taxpayer also relies for conflict (Pet. 12, Br. 22-23), taxpayer merely quotes a brief and unclear portion of the opinion which avowedly

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[1] Section 162 of the Internal Revenue Code, corresponding with the same Section of the 1938 Act here involved, was amended in several respects by Section 111 of the Revenue Act of 1942, c. 619, 56 Stat. 798. By Section 111(e) of the 1942 Act the amendments were made effective for taxable years beginning after 1941. Whatever the changes enacted by these amendments (see *Carlisle* v. *Commissioner,* 165 F. 2d 645 (C.A. 6)) they are not applicable to the taxable year (1939) here involved.

(Pet. 12) is *dictum*. The decision in that case, as well as most of the opinion, confirms the correctness of the holding below, as petitioner impliedly admits (Pet. 25).

CONCLUSION

The decision below is correct, and there is no conflict. The petition for a writ of certiorari should be denied.

Respectfully submitted,

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